

AGNIESZKA McCALEB

CHINA'S AUTOMOBILE INDUSTRY:
DEVELOPMENT, POLICIES,
INTERNATIONALIZATION

China auto industry in only less than fifty years became the world's biggest and currently has the highest growth potential (23 million vehicles sold in 2014)¹. The sector recorded impressive growth considering that between 1950s and 1980s manufacturing focused on military and commercial vehicles and at the end of the 1990s production did not even reach one million vehicles². In 2010, China overtook the United States as the largest market for new cars³.

The automotive market in China is dominated by foreign car producers. Chinese authorities however have an ambitious goal of creating internationally strong domestic car manufacturers. Some of them already made it to the Fortune Global 500 2012 such as Dongfeng Motor, Shanghai Automotive (SAIC), China FAW Group, Zhejiang Geely. In addition, they aim at leapfrogging developed countries by developing new energy vehicles. Both goals are reflected in recent policies that are discussed in this paper. In spite of the impressive growth of car industry in China the country's cars are mainly sold domestically which makes it lag behind the world's top car producers.

The aim of the article is to discuss the development of automotive industry in China, recent policies formulated by the Chinese government that shape China's domestic automotive market. Finally, the article analyses internationalization of Chinese firms from the automotive sector.

¹ *China's car sales growth halves in 2014*, BBC (2015), <http://www.bbc.com/news/business-30775309> (accessed: 14.08.2015).

² A. Amighini, *Chinese FDI in the European Automotive Sector* [in:] *Sustaining Industrial Competitiveness after the Crisis: Lessons from the Automotive Industry*, ed. L. Ciravegna, London 2012, p. 114.

³ McKinsey, *Bigger, better, broader: A perspective on China's auto market in 2020*, http://www.mckinsey.com/client_service/automotive_and_assembly/expertise/emerging_markets (accessed: 14.08.2015).

Overview of China's automotive industry development

At the beginning of the reform period that started at the end of the 1970s, Chinese automotive industry was quite backward. It used Russian and Eastern European technology and designs without really engaging in technological development. Local producers (56 auto assembly plants in 1978) delivered mainly trucks and cars for the government. Chinese leaders chose auto industry to be one of the pillar industries in the Seventh Five Year Plan (1986–1990) as it involved development of many other sectors such as steel, rubber, machinery etc. In the middle of the 1980s, Chinese government's goal was to consolidate the industry to create three large producers and three small ones. They were to form joint ventures (JVs) with foreign producers in order to obtain access to advanced technology, maintain high rates of local content and produce to world standards (i.e. for exports)⁴. In exchange for market access international car producers had to form alliances and JVs with the selected Chinese partners, the practice called “technology for market”⁵. The first JVs for development of passenger cars were established between international investors and local governments: American Motors Corporation (AMC) established a JV in Beijing (1983), Volkswagen in Shanghai (1984), and Peugeot in Guangzhou in 1985. Due to the high domestic market protection, car producers enjoyed high profits and foreign investors were not motivated to introduce new technology. China's preparations for the WTO membership also encompassed the automotive sector. The State Council's Development Research Center issued a report “World Trade Organization and China's Auto Industry”, which concluded that Chinese autos were not competitive (old products, high prices, lack of independent R&D capabilities) due to the protection resulting from the policy of import substitution and small private demand⁶. Chinese policymakers urgently wanted to improve competitiveness of auto industry through promotion of ownership of family cars and reduction of import tariffs. The most important decision however was to allow more intense international competition on the domestic market. Thus, in 1997 Chinese government open the automotive industry to more foreign investors, but required they brought the latest technology. It is important to note that government maintained the policy of prohibiting local companies from entering the industry, which might imply that it did not believe indigenous firms could contribute to the upgrading of the

⁴ E. Thun, *Industrial Policy, Chinese-Style: FDI, Regulation, and Dreams of National Champions in the Auto Sector*, “Journal of East Asian Studies” 2004, p. 458–459.

⁵ R. Tang, *The Rise of China's Auto Industry and Its Impact on the U.S. Motor Vehicle Industry*, <http://www.fas.org/sgp/crs/row/R40924.pdf> (accessed: 12.02.2013).

⁶ WW. Chu, *How the Chinese government promoted a global automobile industry*, “Industrial and Corporate Change” 2011, vol. 20, no. 5, p. 1235–1276.

industry. After WTO entry at the end of 2001, China maintained limit for foreign investors of up to 50% stake in auto assembly companies but allowed 100% ownership by foreign entities in auto parts sector⁷. The inward internationalization process of the auto industry was very intense. By 2002, majority of the global auto manufacturers were present in China such as Toyota, Honda, Nissan, Mazda, Hyundai and Kia⁸.

By 2000, the demand for cars from individual consumers constituted more than 50% of the total and contributed to the growth of indigenous car producers, such as Hafei, Brilliance, Chery (state-owned enterprises, SOEs) and Geely and BYD (private companies), which by 2006 occupied 25% of the domestic car market⁹. At the beginning of 21st century Chery Automobile emerged (SOE governed by Anhui provincial government). Its success made the central government to modify its policy and to start supporting indigenous car producers¹⁰. Thus, the policy of “technology for market” was abandoned and the focus shifted to promotion of indigenous firms and nurturing of national brands. Currently the top 10 car producers (descending order in terms of sold units) are: Shanghai General Motors Company Ltd., Shanghai Volkswagen Automotive Co. Ltd., FAW-VW Automobile Co. Ltd., Dongfeng Nissan Passenger Vehicle Co. Ltd., Beijing Hyundai Motor Company, Chery Automobile Co. Ltd., Geely Holding Group, Chang'an Ford Automobile Co. Ltd., Dongfeng Peugeot Citroen Automobile Company Ltd., FAW Toyota Motor Sales Co. Ltd.¹¹, which shows that JVs with foreign automakers maintain a strong position on the Chinese market.

Major automotive industry policies since 2004

The auto industry policies are manifestation of the government's wish to monitor and develop the industry. Since the beginning of reforms there were many changes to the agencies that govern the auto industry policy. Currently, industrial policy body under National Development and Reform Commission (NDRC) has a unit that manages policies related with the auto industry. The State-owned Assets Supervision and Administration Commission (SASAC) governs major SOEs such as FAW,

⁷ *Ibidem*.

⁸ A. Amighini, *Chinese FDI...*, p. 114–133.

⁹ WW. Chu, *How the Chinese government...*, p. 1235–1276.

¹⁰ Chery was so successful that it became officially listed as a state project and had obtained increased state support. An example, in 2005 the Ministry of Science and Technology (MOST) decided to establish “National Automobile Engineering Technology Research Center of Energy Saving and Environmental Protection” at Chery's Automobile Engineering Research Institute. *Ibidem*, p. 1257.

¹¹ http://www.china.org.cn/top10/2012-02/10/content_24604448_10.htm (accessed: 10.08.2015).

SAW as well as China Automotive Technology and Research Center that is in charge of R&D works¹². China Association of Automobile Manufacturers is a semi-official organization that is in charge of policy and coordination works.

In June 2004, NDRC issued “Automotive Industry Development Policy” that was to put it in line with WTO obligations and set the guidelines for the development of the industry. Its aim was to develop large-scale automakers, consolidate the sector, support creation of domestic components industry, encourage conducting R&D activities locally, develop indigenous intellectual property, and implement branding strategy¹³. Moreover, the new policy introduced high entry barriers to companies from outside the automotive industry, which was motivated by fears of overinvestment in the industry that might have led to overcapacity and reduced margins. Thus, local and foreign auto manufacturers were supported. The 2004 policy also ended the requirement for local content and export, simplified administrative procedures, encouraged energy saving and environmental protection etc. However, government maintained its role as a guide for industrial structure mainly through its tool of granting an entry approval but also through guiding mergers and restructuring¹⁴.

The global financial crisis of 2008 pushed Chinese authorities to support the automotive industry through “Automotive Industry Readjustment and Revitalization Plan” issued in March 2009. It was a three-year plan for the auto industry that further encouraged the industry to consolidate and restructure. As a result of the plan the sales grew substantially by 45% in 2009 and 32% in 2010¹⁵.

Important policy change was reflected in regularly published by NDRC “Foreign Investment Catalogue” where foreign investments are divided into four categories: encouraged, permitted, restricted and prohibited. In the 2011 edition automobile producers were removed from “encouraged” list while new energy vehicles were placed on “encouraged” list¹⁶. In the latest issue of 2015 the production of complete automobiles was moved to “restricted” category. This shift means a hindrance to foreign companies that were not yet present in China but intended to do so. However, investment related with manufacturing of engines and other key parts, R&D in key technologies, batteries and electric motors for new energy vehicles are

¹² WW. Chu, *How the Chinese government...*, p. 1235–1276.

¹³ *Ibidem*.

¹⁴ *Ibidem*.

¹⁵ J. Ribera Segura, M. Sachon, T.E. Callarman, H. Li, X. Shen, C. Castillo, *What's Driving China's Auto Industry?*, China Europe International Business School 2014, <http://www.ieseinsight.com/doc.aspx?id=1691&ar=14> (accessed: 14.08.2015).

¹⁶ R. Tang, *China's Auto Sector Development and Policies: Issues and Implications*, “Congressional Research Service” 7–5700, 2012.

still encouraged¹⁷. This way the government wants to strengthen domestic producers and attract technology the industry, especially in new energy vehicles.

China issued Energy-Saving and New-Energy Auto Industry Plan (2012–2020) in order to develop new energy automotive sector. It serves as a guideline for more specific regulations concerning this sector while showing the ambition to leapfrog developed countries in this domain. The current 12th Five Year Plan (2011–2015) also emphasizes the importance of new energy auto industry as it was chosen to be one of its seven strategic emerging industries. The Chinese authorities have the ambition for their domestic manufacturers to become “market leaders in e-mobility”¹⁸.

Internationalization of Chinese automotive companies

Chinese automakers' overseas operations are not only an important step to expand in the global market, but also a natural choice for the companies' self development... We should encourage their outbound investments and support them to increase their capital exports to overseas markets.

Chen Lin (2012)

MOFCOM, Department of Outward Investment and Economic Cooperation¹⁹

The exports of Chinese passenger car manufacturers are considerably small showing slight growth only in 2010 (figure 1). In 2014, China exported 4.5 billion USD of passenger cars which was more than Brazil (3 billion), but less than India (5.7 billion) and not to mention Canada's exports worth 44.8 billion USD (the world's fifth largest car exporter) and Germany, the world's biggest exporter of cars, whose passenger cars exports accounted for 160 billion USD²⁰. China mostly exports light trucks and passenger cars to developing countries (mainly Russian Federation and Ukraine). Majority of Chinese car exports are vehicles produced by independent private producers such as Chery and Geely which are sold for less than 10,000 USD in developing countries²¹ (figure 2). Most of Chinese passenger car exports are directed to the Middle East which accounts for half of the ten top export destina-

¹⁷ T. Han, *Foreign auto investment no longer 'encouraged'*, “China Daily”, 9.01.2012, http://www.chinadaily.com.cn/bizchina/2012-01/09/content_14407434.htm (accessed: 20.02.2013).

¹⁸ E-mobility – electrically-powered vehicles. M. Meissner, *E-mobility: China planning fresh start for domestic automobile industry*, Mercator Institute for China Studies, “China Monitor” 2014, no. 17, http://www.merics.org/fileadmin/templates/download/china-monitor/China_Monitor_No_17_en.pdf (accessed: 14.08.2015).

¹⁹ F. Li, *Chinese automakers build overseas plants*, “China Daily”, 15.08.2012. http://www.chinadaily.com.cn/business/overseascnep/2012-08/15/content_15897221.htm (accessed: 14.08.2015).

²⁰ UN Comtrade Database.

²¹ A. Amighini, *China and India in the international fragmentation of automobile production*, “China Economic Review” 2012, no. 23, p. 325–341.

tions²². China's negligible size of car exports is mainly due to the fact that foreign companies were and are not interested in supporting local firms' exports ambitions. However, China is now the world's fifth-largest exporter of auto parts and accessories, the exports of latter grew at 28% annually since 1995 (figure 3). In 2011, a share of domestic producers in Chinese domestic automotive market dropped from 46% in 2010 to 44% in 2011, but exports grew by 59%²³. It is important to note the imports of passenger cars that drastically exceed the exports (figure 1) which is due to the fact that Chinese consumer prefer imported cars over the ones produced domestically.

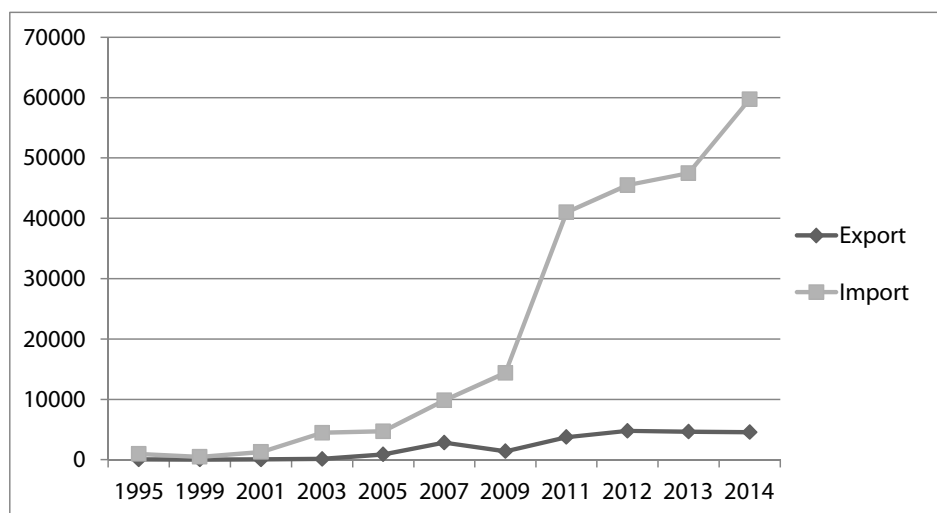


Figure 1. China's export and import of passenger cars (HS8703) in 1995–2014, UN Comtrade database (USD mln)

Source: UN Comtrade database (14.08.2015).

The launch of Go Global Policy at the beginning of the 2000s pushed China's automotive companies to expand into foreign markets. Since 2003 till the end of 2012, China auto producers expanded abroad in more than 27 countries establishing 546 companies and institutes²⁴. Automotive sector was on the third position within manufacturing in terms of OFDI (8% of total Chinese OFDI since 2003)²⁵.

²² R. Drauz, *In search of a Chinese internationalization theory*, "Chinese Management Studies" 2013, vol. 7, Issue 2, p. 281–309.

²³ *China will größter Autoexporteur der Welt werden*, "Frankfurter Allgemeine Zeitung", 24.10.2012, Nr. 248, seite 17.

²⁴ F. Li, *Chinese automakers...*

²⁵ A. Amighini, *Chinese FDI...*, p. 114–133.

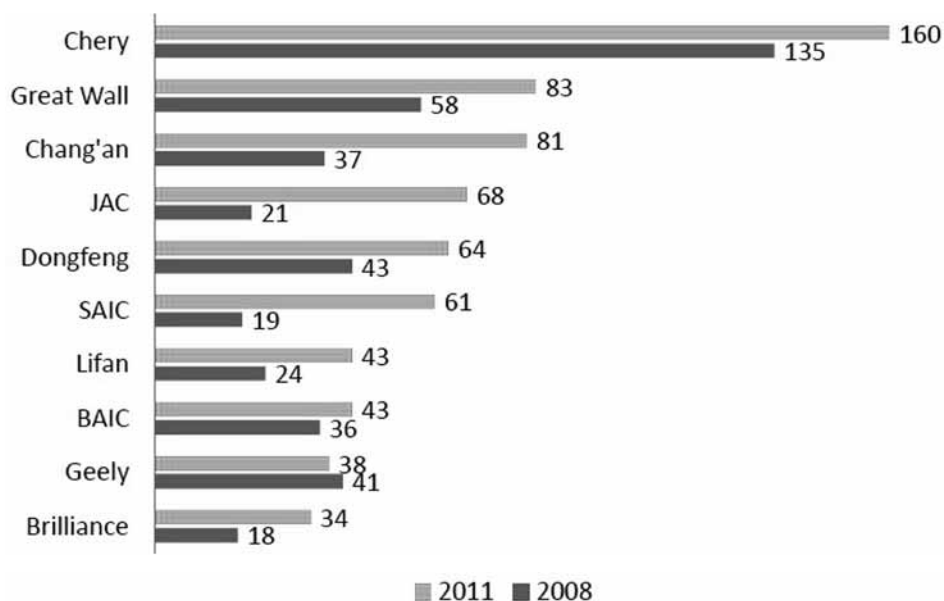


Figure 2. Passenger car exports by China's main domestic producers in 2011 and 2008, in thousand pieces

Source: "Frankfurter Allgemeine Zeitung", 24.10.2012.

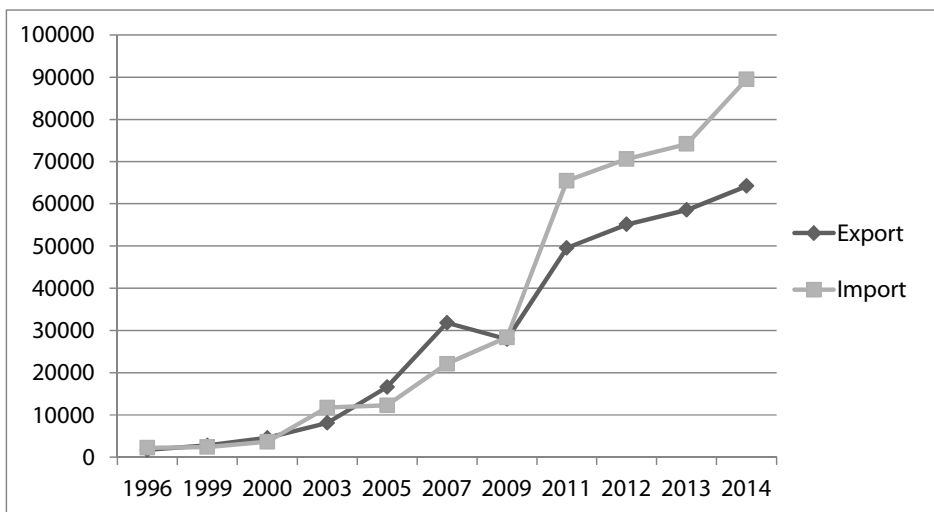


Figure 3. China, exports and imports of vehicles and their parts in 1995–2014, excluding railway, HS87, USD mln

Source: UN Comtrade database (14.08.2015).

Majority of OFDI between 2003 and 2008 was undertaken by original equipment manufacturers (70%), and remaining part by components suppliers²⁶. Foreign investments in developing countries aimed at securing access to new markets where customers accept rather unknown Chinese brands and the level of quality and safety of Chinese cars. The most favored destinations however seem to be developed countries with Europe taking the lead with 38% of OFDI followed by North America (12%), Japan (12% out of total 30% of OFDI in Asia), 9% in Africa and Latin America each²⁷. In developed countries Chinese companies search for access to advanced technologies that would enable Chinese producers to compete with established global players not only internationally but especially on the domestic market. From the beginning of 2009 till the end of the first half of 2010, 11 deals were concluded which is impressive growth when compared with only 12 in the period 2005–2008²⁸. Only in 2009 there were several deals concluded that drew attention of the public in the host countries such as BAIC acquisition of SAAB, Tengzhong's of the American Hummer and Geely's of Volvo. This wave of acquisitions caused fears abroad of China "buying a car industry"²⁹. In Europe, Chinese automotive firms' investments are concentrated in a small group of countries that have high technological capabilities in the sector such as Belgium, Germany, Italy, Sweden and the UK³⁰. The motivations behind investments in these countries are asset-seeking and strategic asset-seeking, including R&D, design and product development. Investments in foreign firms aimed at boosting Chinese companies' research and development capacities are commonly commented as being "in line with the government's call for domestic carmakers to go abroad and seek solid technological resources"³¹ (China Daily, 22.10.2012). Investments in Central, Eastern and Southern Europe are motivated by market-seeking motivations.

As to OFDI motivations of Chinese automakers Amighini³² found, providing only qualitative analysis which is due to the limitations of the dataset, that Chinese companies from automotive sector in their OFDI decisions are mainly driven by technological determinants (strategic asset-seeking, such as intellectual prop-

²⁶ A. Amighini, *The international expansion of Chinese auto firms: typology and trends*, "International Journal of Automotive Technology and Management" 2012, vol. 12, no. 4, pp. 345–359.

²⁷ A. Amighini, *Chinese FDI...*, p. 114–133.

²⁸ E. An, *Overseas acquisitions by Chinese companies offer rewards and risks*, "China Daily", 14.01.2011, http://www.chinadaily.com.cn/hkedition/2011-01/14/content_11850205.htm (accessed: 12.02.2013).

²⁹ M. Schuman, *China is Trying to Buy a Car Industry*, "Time", 17.03.2014, <http://time.com/26840/china-buying-foreign-car-makers/> (accessed: 14.08.2015).

³⁰ A. Amighini, *Chinese FDI...*, p. 114–133.

³¹ T. Han, *Dongfeng looks overseas for R&D*, "China Daily", 22.10.2012, http://www.chinadaily.com.cn/bizchina/2012-10/22/content_15835901.htm (accessed: 20.02.2013).

³² A. Amighini, *Chinese FDI...*, p. 114–133.

erty rights, high technology exports, amount of labor force with tertiary education, number of publications in scientific journals) and only partially by economic (GDP or GDP per capita, cost of labor, abundance of natural resources in host country, fiscal pressure in the host country) and institutional factors (institutional distance, quality of regulatory framework, cultural distance). Amighini argues that agglomeration effect exists in Chinese auto producers' OFDI as they tend to locate where Chinese companies from other sectors operate. Amighini also claims that this 'national factor' is "easily explained in a political economy setting as the result of the efforts made by the Chinese business diplomacy, which usually pave the way for Chinese FDI in a number of sectors". Agglomeration effect is also visible at the sector level as Chinese auto firms prefer to locate where other automotive companies invest in order to benefit from knowledge spillovers resulting from clustering of firms from the same sector.

The companies from auto industry in China are commonly divided into SOEs and independent manufacturers (自主品牌, *zìzhǔ pǐnpái*). Independent manufacturer means a private firm that is not engaged in JVs with foreign counterparts. As of 2015, the major foreign investors were state-owned companies such as Chery Automobile (14 FDI projects, 3 R&D units abroad), Nanjing Automobile Group (independent till 2007 when it merged with SAIC) (9 FDI), Chang'an Automobile Group (4 FDI, 4 R&D units abroad) and independent producers included Great Wall Motors (6 FDI) and Geely (5 FDI). The study done by Drauz³³ confirms the most internationalized Chinese automakers are Chang'an, Chery and Great Wall Motors.

Many of the foreign plants owned by Chinese automotive firms are managed by the local partners³⁴. It is confirmed by the Polish case of FLT Krasnik acquired by the Chinese Tri Ring Corporation in August 2013 that is fully operated by the Polish management. The company produces different types of bearings for automotive industry. It seems that the Chinese investor was primarily interested in obtaining access to the European automotive market for parts and components. This strategic approach enables Chinese company to benefit and learn from its foreign partner about the local market.

Conclusion

The automotive industry in China seems to be bound for success taking into consideration huge domestic market and the support provided by the government. The policies introduced by the Chinese authorities show their understanding of the importance of the automotive industry for the growth of the whole economy. We

³³ R. Drauz, *In search of a Chinese...*, p. 281–309.

³⁴ *Ibidem*.

should expect from Chinese authorities and companies intensified efforts aiming to improve quality and safety of the domestically produced cars as well as increased works towards brand building. The latter is significant barrier to sales domestically where Chinese firms compete with well-established global brands that are favored by Chinese consumers but also in developed markets and higher market segments.

Chinese automobile companies in their internationalization mainly search for technology they lack to become competitive on both domestic and international markets. The analysis of their website shows their dedication to research and development, for example Great Wall states “we have kept to a strategy of “excessive investment in technical R&D”. Majority of companies engage in development of new energy cars which seems to be primarily result of the government’s policy on fostering emerging industries.

Although Chinese automakers face many challenges but we should prepare ourselves that in the near future we will be driving Chinese cars.

STRESZCZENIE

CHIŃSKI PRZEMYSŁ MOTORYZACYJNY – ROZWÓJ, POLITYKI, INTERNACJONALIZACJA

Chiński przemysł motoryzacyjny szybko rozwinął się od czasu otwarcia kraju na początku lat 80. XX wieku Chińscy producenci samochodów skorzystali z wewnętrznej polityki rządu w zakresie bezpośrednich inwestycji zagranicznych, które ułatwiły dostęp do technologii wprowadzanych na wewnętrzny rynek przez międzynarodowe korporacje z branży motoryzacyjnej. W ostatnich latach Chiny stały się największym rynkiem samochodów na świecie. Celem artykułu jest omówienie rozwoju przemysłu motoryzacyjnego w Chinach, bieżących zasad i strategii sformułowanych przez chiński rząd, które kształtują krajowy rynek motoryzacyjny w Chinach. W ostatniej części artykułu dokonano analizy zagadnienia internacjonalizacji chińskich firm z branży motoryzacyjnej.